



CALIFORNIA BOARD OF ACCOUNTANCY

2000 EVERGREEN STREET, SUITE 250
SACRAMENTO, CA 95815-3832
TELEPHONE: (916) 263-3680
FACSIMILE: (916) 263-3675
WEB ADDRESS: <http://www.dca.ca.gov/cba>



Final Statement of Reasons

Related to Regulation Change Notice from UPDATE #54

October 23, 2003

Hearing Date: July 25, 2003

Sections Affected: Sections 12, 12.5, 87, 87.1, and 90 of Division 1 of Title 16 of the California Code of Regulations.

Updated Information:

The Initial Statement of Reasons is included in the file. The information contained therein is updated as follows:

The public hearing was held on July 25, 2003, in Burlingame CA. No one appeared to testify at the hearing. After the hearing, the Board took action with regard to the proposal.

During the comment period, one letter was received related to the proposed revisions to Sections 12 and 12.5. This comment letter, from Mr. Paul Korneff, expressed concern that the proposed revisions would require that a separate verification of the applicant's experience be completed by each direct supervisor. In those instances in which the applicant has several direct supervisors at a firm or agency, Board staff would need to review and process several verifications of experience instead of the single verification submitted by the firm under current requirements.

After considering this comment, the Board adopted the originally proposed text for Sections 12 and 12.5 because the Board concluded that inquiries from licensees and applicants are likely to decrease as a result of having a clear definition of supervision that is uniformly applied. This decreased workload is likely to offset additional workload created by multiple verifications.

During the comment period, one letter was received commenting on the proposed revisions to Section 87, 87.1, and 90. The commenter expressed support for the concept of requiring continuing education related to fraud detection, but indicated he believed the language was unclear as to whether all eight hours of this continuing education must be related to fraud detection or whether the continuing education could be in "reporting on financial statements."

To address this concern the Board adopted the following revisions to Sections 87 and 87.1:

(d) A licensee who must complete continuing education pursuant to subsections (b) and/or (c) of this section shall also complete an additional eight hours of continuing education ~~in detecting fraud affecting~~ **specifically related to the detection and/or reporting of fraud in** financial statements ~~or reporting on financial statements~~. This continuing education shall be part of the 80 hours of continuing education required by subsection (a), but shall not be part of the continuing education required by subsection (b) or (c). This requirement applies to licensees who renew their licenses ~~on or~~ after July 1, 2004.

Two additional minor revisions were adopted by the Board: 1) Sections 87 and 87.1 were revised to clarify that the fraud continuing education requirement would apply to licenses renewed or converted to active status “on or “after” July 1, 2004, and 2) Section 90 was updated to reference Section 5100(g) instead of (f) to reflect the recent relettering of Business and Profession Code Section 5100.

After the hearing, the Board adopted modified language described above for Sections 87, 87.1, and 90 pending a 15-day public comment period. The Board delegated to its President the authority to approve the final language provided no adverse comments were received. The modified text was made available for public comment during the period August 15, 2003, through September 5, 2003. The modified text was also posted on the Board’s Web site. No comments were received.

After the public comment period and the Board’s action on the proposal, another comment letter was received requesting that the proposal be modified to include the eight hours of fraud continuing education as part of the required 24 hours of accounting and auditing continuing education. This recommendation was not accepted because, during its initial policy evaluation of fraud continuing education, the Board concluded that 24 hours of accounting and auditing continuing education was critical, and therefore eight hours of fraud continuing education should be required in addition to the accounting and auditing continuing education requirement. Even though this comment letter was received after the comment period, a copy of the modified text was sent to the commenter giving him an opportunity to comment on the modifications.

Local Mandate:

A mandate is not imposed on local agencies or school districts.

Small Business Impact:

The California Board of Accountancy has determined that this regulatory action will not have a significant adverse effect on small businesses.

Proposed revisions clarify requirements related to the supervision of applicants for licensure, but establish no new requirements. Proposed eight hours of fraud detection continuing education would be part of the 80 hours currently required for license renewal. The total number of continuing education hours would not change.

Consideration of Alternatives:

No reasonable alternative which was considered or that has otherwise been identified and brought to the attention of the Board would be either more effective in carrying out the purpose for which the action is proposed or would be as effective and less burdensome to affected private persons than the proposed regulations.

The Initial Statement of Reasons discussed proposed alternatives and why they were rejected. In addition, the originally proposed text for Sections 87, 87.1 and 90 was

rejected in favor of the modified text for the reasons discussed above in “Updated Information.”

Objections or Recommendations/Responses:

1. May 30, 2003, e-mail from Steve Nash, CPA. The commenter indicated that the originally proposed text related to fraud continuing education was unclear as to whether all eight hours of continuing education must be related to fraud or whether it could be in “reporting on financial statements.” The commenter suggested alternative language to clarify that all eight hours of continuing education should be related to fraud affective financial statements. He expressed support for the concept embodied in the proposal indicating that it is appropriate since the public expects a CPA to detect financial statement fraud.

The Board’s Response: The Board agreed with the commenter’s concern. While the Board did not adopt specific language suggested by the commenter, the Board did adopt the following revisions to Sections 87 and 87.1 which are consistent with the concept embodied in his suggestions:

(d) A licensee who must complete continuing education pursuant to subsections (b) and/or (c) of this section shall also complete an additional eight hours of continuing education ~~in detecting fraud affecting specifically related to the detection and/or reporting of fraud in financial statements or reporting on financial statements.~~ This continuing education shall be part of the 80 hours of continuing education required by subsection (a), but shall not be part of the continuing education required by subsection (b) or (c). This requirement applies to licensees who renew their licenses ~~on or~~ after July 1, 2004.

2. A July 15, 2003, letter from Paul Koreneff. The commenter noted that the proposed regulation requires that the verification of experience (Form E) be signed by both the supervisor and a more senior representative of the employer. On consequence is that there must be a separate verification for each direct supervisor. The commenter indicated that in a public accounting firm, over a two-year period, there may be as many as 20 different supervisors. He indicated that for applicants transferring from another state, there may be over 100 direct supervisors. He suggested that this would be significant increase in the number of verifications that would need to be processed with each application. Also, there may be instances in which the direct supervisor is no longer available to sign the verification. In prior years, firms could summarize the candidate’s experience on one verification. He added that under the proposal, staff would need to prepare the summary instead.

The commenter indicated that, under the proposed revisions, employers will prepare verifications only for the minimum period required for licensure with the right to issue attest reports. He suggested this would restrict the information gathered by the Board related to a candidate’s experience and would restrict the ability of staff to select candidates whose experience needed to be reviewed by the Board’s Qualifications Committee.

He recommended that Sections 12 and 12.5 be revised to permit an owner or partner of a licensed firm to summarize the applicant's experience on one verification. If that owner or partner was asked to appear before the Board's Qualification's Committee, he or she would be required to show support for the statements on the verification.

He added that a similar situation for applicants for a general license (no attest experience required).

The Board's Response: The commenter's recommendation was rejected for several reasons. The commenter indicated that the proposal would result in an increase in the number of verifications received by the Board and therefore an increase in the staff time involved in processing these applications. First, the Board observed that, at this time, it is not possible to accurately estimate any increase in the number of verifications that will be received under the revised regulations. However, it appears that the commenter probably provided a high-end estimate of the increased volume by giving consideration only to those public accounting firms that employ numerous licensees as supervisors. Further, the Board concluded that the number of inquiries from licensees and applicants is likely to decrease as a result of having a clear definition of supervision that is uniformly applied. This decreased workload is likely to offset additional workload created by any multiple verifications which Board staff will need to review and summarize.

With regard to the commenter's concern that the direct supervisor may no longer be available to sign the verification, the Board agrees this is an important concern, but notes that this can be the case under current requirements as well as under the revised requirements. It is for this reason that the Board encourages applicants to obtain the required verifications promptly after completing the required experience.

The commenter further suggested that the new requirements might encourage employers to verify only the minimum experience required for licensure with the right to issue attest reports. He suggested that this will restrict the information about the applicant available to the Board. If this occurs, it is unclear how the applicant or the Board would be disadvantaged since it is only necessary for the applicant to demonstrate that he or she meets the Board's minimum requirements.

To address the concerns he described, the commenter recommended that Sections 12 and 12.5 be revised to permit an owner or partner of a licensed firm to summarize the applicant's experience on one verification. This recommendation was rejected by the Board because it would result in the inconsistent application of the definition of supervision added to Sections 12 and 12.5 by this proposal. Under this recommendation, different verification requirements would apply to experience obtained in private industry or government compared with experience obtained at a public accounting firm. In addition to creating concerns related to equity and the uniform application of

requirements, this inconsistency is likely to be confusing to applicants and licensees and result in increased inquiries which must be answered by Board staff.

The commenter concluded by indicating that a similar situation exists for applicants applying with general as well as with attest experience. The Board concurs and believes the same reasons for rejecting the commenter's recommendations apply.

3. August 5, 2003, e-mail from Samuel V. Ortiz. The commenter indicated that he did not object to the mandate that licensee's complete continuing education related to fraud detection. However, he believed the proposal did not consider that the majority of California CPAs are sole practitioners or work for very small firms. He objected to requiring fraud continuing education in addition to 24 hours of accounting and auditing. He suggested that sole practitioners and small firms perform few accounting/auditing engagements, but would now need to dedicate 40 percent of their continuing education to accounting and auditing issues. He noted that in those years when an ethics and professions conduct course is required, 50 percent of the licensee's continuing education would be in these subject areas. He suggested this is overweighted and does not leave an appropriate number of hours in areas more directly related to the licensee's practice.

The commenter recommended that the proposal be modified to allow the fraud continuing education to be part of the 24 hours of required accounting and auditing continuing education. He suggests that this would allow the sole practitioner or small firm to spend their continuing education dollars more appropriately.

The Board's Response: This recommendation was rejected because the Board concluded that 24 hours of accounting and auditing continuing education was critical, and therefore eight hours of fraud continuing education should be required in addition to the accounting and auditing continuing education requirement. It was not the Board's intent to ignore the needs to sole practitioners and small firms. Instead, the Board's goal has been to establish uniform requirements that benefit California's consumers.